



AUDITOR - GENERAL

The Municipal Manager
Umgungundlovu District Municipality
P.O. Box 3235
PIETERMARITZBURG
3200

18 December 2007

Reference: 21470REG06-07

Dear Dr MN Mngadi

Report of the Auditor-General on the financial statements and performance information of the uMgungundlovu District Municipality for the year ended 30 June 2007

The above-mentioned report of the Auditor-General are submitted herewith in terms of section 21(1) of the Public Audit Act, 2004 (Act No. 25 of 2004 read in conjunction with section 188 of the Constitution of the Republic of South Africa, 1996 (Act No. 108 of 1996) and section 121(3) of the Municipal Finance Management Act, 2003 (Act No. 56 of 2003)(MFMA)

In terms of section 121(3) and 127(2) of the MFMA municipalities have to include the audit report in the municipality's annual report for tabling within seven months after the end of the financial year.

Until tabled as required by section 127(2) the report is **not a public document** and should therefore be treated as **confidential**.

As your municipality will be responsible for publishing the attached audit report as part of the annual report, you are required to do the following:

- Submit the final printer's proof of the annual report (which includes the audit report) to the relevant audit manager of the Auditor-General for verification of the audit-related references before it is printed or copied. Special care should be taken with the page references in your report, since an incorrect reference could have audit implications.
- The signature at the end of the hard copy of the audit report should be scanned in when preparing to print the report. The signature Auditor-General in the handwriting of the auditor authorised to sign the audit report, as well as the place and date of signing and the logo should also appear at the end of the report, as in the hard copy that is provided to you. The official logo and the authorised signature will be made available to you in electronic format.

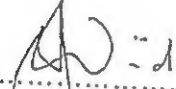
Please notify the Provincial Auditor-General (Business Executive) well in advance of the date on which the audit report, or the annual report containing this audit report, will be tabled at the municipality.

Your cooperation to ensure that all these requirements are met would be much appreciated.

Kindly acknowledge receipt of this letter.

Yours sincerely

Signed


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**REPORT OF THE AUDITOR-GENERAL TO THE MUNICIPAL COUNCIL AND
KWAZULU-NATAL PROVINCIAL LEGISLATURE ON THE FINANCIAL
STATEMENTS AND PERFORMANCE INFORMATION OF UMGUNGUNDLOVU
DISTRICT MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2007**

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I was engaged to audit the accompanying financial statements of the Umgungundlovu District Municipality which comprise the balance sheet as at 30 June 2007, income statement and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages 6 to 19.

Responsibility of the accounting officer for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the entity-specific basis of accounting, as set out in accounting policy note 1 to the financial statements and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA). This responsibility includes:
 - designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error
 - selecting and applying appropriate accounting policies
 - making accounting estimates that are reasonable in the circumstances.

Responsibility of the Auditor-General

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA) and section 126(3) of the MFMA, my responsibility is to express an opinion on these financial statements based on my audit in accordance with the International Standards on Auditing. Because of the matters discussed in the Basis for disclaimer of opinion paragraphs, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis of accounting

4. The municipality's policy is to prepare financial statements on entity-specific basis of accounting as set out in accounting policy note 1 to the financial statements.

Basis for disclaimer of opinion

Water services transactions

5. Income and expenditure of R35,4 million and R36,6 million respectively, relating to water services provided by Impendle, uMshwathi, uMngeni and Mpofana

municipalities on behalf of the district municipality was not supported by valid documentation.

Furthermore, the service level agreements between the district municipality and the local municipalities for the supply of water and sanitation services on behalf of the district municipality could not be produced for audit purposes.

Consequently, I was unable to satisfy myself as to the validity, accuracy or completeness of income and expenditure of R35,4 million and R36,6 million respectively.

Payables

CBPWP balance

6.1 No supporting documentation could be provided to support the outstanding balance of R4,2 million in respect of the Community Based Public Works Programme. As a result, I could not satisfy myself as to the valuation or municipality's obligation to settle this liability.

Consumer deposits

6.2 No schedule or list of consumer deposits could be provided to support the balance of R2,3 million included in the financial statements. This amount is made up of consumer deposits held by the various municipalities acting as agents on behalf of Umgungundlovu District Municipality. As a result, I could not satisfy myself as to the accuracy or completeness of the consumer deposits balance of R2,3 million.

Unspent conditional grants incorrectly accounted for

6.3 An amount of R17 million received in respect of conditional grants was incorrectly included directly in income for the year and the related expenditure was incorrectly included in expenditure. This is contrary to recognised accounting principles, as these funds meet the definition and recognition criteria of a liability as the unspent portion may be refundable to the donor, unless the conditions attached to the grants are met.

As a result, creditors are materially understated by an unknown amount and the accumulated surplus, income and expenditure are overstated.

Capital commitments

7. Supporting documentation in respect of the capital commitments balance of R216 million as disclosed in note 25 to the annual financial statements could not be provided. As a result, I was unable to satisfy myself as to the validity or accuracy of the capital commitments of R216 million.

Receivables

Unconfirmed water debtors

8.1 Included in sundry debtors is an amount of R85,4 million relating to water services performed by the local municipalities appointed as agents for which no supporting schedules could be provided.

As a result, I could not verify the existence or recoverability of the above balance.

Long outstanding debtors

8.2 Included in other debtors is an amount of R1,7 million dating back to 1996 and against which no movement has been noted. As a result, I could not satisfy myself as to the valuation and recoverability of these debtors.

Provision for bad debts

8.3 Management's basis for the provision for bad debts of R80 million (2006: R71 million) or supporting documentation for the calculation could not be provided. Furthermore, included in other debtors of R133 million is an amount of R85 million relating to water debtors managed by the local municipalities providing water services on behalf of the district municipality and for which no debtors age analysis could be provided to reasonably determine what the provision should have been. As a result, I could not satisfy myself as to the reasonability or completeness of the provision for bad debts of R80 million.

Material losses through fruitless and wasteful expenditure

Councillor cell phone allowances

9. Councillors were paid cell phone allowances in addition to having cell phone accounts being settled by the municipality. In the absence of separate accounting records relating to cell phone accounts, I was unable to determine the extent of overpayments made to councillors which has not been disclosed as fruitless and wasteful expenditure in the financial statements, as required by section 125(2)(d)(i) of the MFMA.

Provisions

Provision for leave pay

10. A difference of R1 million exists between the leave pay provision as per the financial statements and the amount recalculated from the leave balances as per the leave system.

Furthermore, leave files and leave records requested for audit were not provided, therefore the validity, accuracy and completeness of the leave balances used in the calculation of the leave pay provision could not be verified. As a result, I could not satisfy myself as to the completeness and valuation of the leave provision of R2,4 million.

Fixed assets

Fixed asset register

11.1 A complete fixed assets register including sufficient details could not be provided for audit. Furthermore, no supporting documents could be provided to validate the asset count performed during the year. Therefore, I could not satisfy myself as to the existence, completeness and valuation of the fixed assets of R130 million.

Capital projects

11.2 Information relating to project expenditure and contract agreements could not be provided. The related accounting and internal controls did not permit alternative audit procedures therefore I could not satisfy myself as to the completeness or valuation of capital projects included in fixed asset additions.

Physical verification not possible

- 11.3 Fixed assets totalling R144 million relating to sewerage and water works, taken over on transfer of water services to the district municipality, could not be physically verified as no supporting documentation or detailed schedules could be provided for audit purposes. As a result, I could not satisfy myself as to the existence of these assets.

Incorrect accounting policy

- 11.4 Fixed assets are incorrectly depreciated over their estimated useful lives instead of being depreciated in accordance with its funding source. Furthermore, Appendix C to the financial statements do not disclose any movement on loans redeemed and other capital receipts even though fixed asset additions of R26,7 million have been recorded.

Borrowings

Balance does not agree to confirmation

- 12.1 Confirmation of balances obtained directly from the Development Bank of South Africa (DBSA) revealed a difference of R1 million in excess of the amount confirmed by DBSA.

As a result, long term liabilities are overstated by R1 million.

DC 29 liability not supported

- 12.2 The long term liability in respect of DC 29 carried forward from the previous year of R120 000 as per note 2 to the financial statements could not be substantiated by any valid documentation. It could also not be ascertained what the liability relates to. As a result, I could not satisfy myself as to the validity and municipality's obligation to settle this debt.

Accumulated surplus

Lack of information

- 13.1 Supporting documentation and related schedules for the appropriations totalling R3,5 million as per note 15 to the financial statements could not be provided for audit. As a result, I could not satisfy myself as to the validity or accuracy of the net appropriations of R3,5 million processed against the accumulated surplus.

Disclaimer of opinion

14. Because of the significance of the matters described in the Basis for disclaimer of opinion paragraphs, I have been unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements of the Umgungundlovu District Municipality. Accordingly, I do not express an opinion on the financial statements.

Emphasis of matter

15. I draw attention to the following matter:

Sisonke District Municipality loan account

16. An amount of R8,6 million disclosed as Loan account – Sisonke District Municipality is owed by Sisonke District Municipality. This debtor arose from the demarcation transaction process and is still under discussion and in dispute. Attention is also drawn to note 7 to the financial statements in this regard.

OTHER MATTERS

I draw attention to the following matters that are ancillary to my responsibilities in the audit of the financial statements:

Non-compliance with applicable legislation

Municipal Finance Management Act

17. The following non-compliance with the MFMA were identified:

- Disclosure in respect of taxes (VAT), pension and medical aid contributions was not included in the financial statements as required by section 125 (1) (c) of the MFMA.
- Details of all bank accounts as required by section 125 (2) (a) of the MFMA was also not disclosed in the notes to the financial statements.
- Payments totalling R479 000 was not made within 30 days of the invoice date as required by section 65(2) (e) of the MFMA.

Supply Chain Management Regulations (SCMR)

18. Declarations of any conflicts of interests by bidders in respect of awarded contracts were not made as required by paragraph 21(c) of the Supply Chain Management Regulations, which compels bidders to declare any conflict of interest that they may have in the transaction in respect of any bid submitted.

Internal control

19. Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes of the matters indicated, as they relate to the five components of internal control. In some instances deficiencies exist in more than one internal control component.

Reporting item	Control environment	Assessment of risks	Control activities	Information and communication	Monitoring
Basis for disclaimer of opinion					
Water services transactions Water			✓		
Payables			✓		
Capital commitments			✓		✓

Reporting item	Control environment	Assessment of risks	Control activities	Information and communication	Monitoring
Receivables			✓		
Expenditure					✓
Provisions					✓
Fixed assets			✓		✓
Borrowings					✓
Accumulated surpluses			✓		
Other matters					
Non-compliance with applicable laws and regulations			✓		

Unaudited supplementary schedules

20. The supplementary information set out on pages 20 to 25 do not form part of the financial statements and is presented as additional information. I have not audited these schedules and accordingly I do not express an opinion on them.

OTHER REPORTING RESPONSIBILITIES

Reporting on performance information

21. I was engaged to audit the performance information.

Responsibility of the accounting officer for the performance information

22. In terms of section 121(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality prepared by the municipality in terms of section 46 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).

Responsibility of the Auditor-General

23. I conducted my engagement in accordance with section 13 of the PAA read with General Notice 646 of 2007, issued in Government Gazette No. 29919 of 25 May 2007 and section 45 of the MSA.
24. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.

25. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

Audit findings (performance information)

Non-compliance with regulatory requirements

Performance Management System framework not approved by council

26. A framework that describes and represents how the municipality's cycle and process of performance planning, monitoring, measurement, review, reporting and improvement will be conducted, organised and managed, including determining the roles of the different role-players, as required by regulation 7(1) of the Local Government: Municipal Planning and Performance Management Regulations, 2001, does not exist.

Approval of Service Delivery Budget Implementation Plan (SDBIP)

27. The SDBIP was not approved by the mayor within 28 days of approval of the budget as required by section 53 (1)(c) of the MFMA.

No monitoring of performance information

28. The requirements for monitoring, measurement and review as stipulated in regulation 13 of the Local Government: Municipal Planning and Performance Management Regulations, 2001, have not been complied with.

Performance information not received

29. The municipality did not submit the annual performance report as required by section 46 of the MSA. Consequently, the annual performance information, to be included in the annual report of the municipality, was not audited.

No performance contracts

30. Managers appointed in terms of section 57 of the MSA did not sign performance contracts in accordance with section 57 of the MSA.

APPRECIATION

31. The assistance rendered by the staff of the Umgungundlovu District Municipality during the audit is sincerely appreciated.

Auditor-General

Pietermaritzburg

14 December 2007



A U D I T O R - G E N E R A L